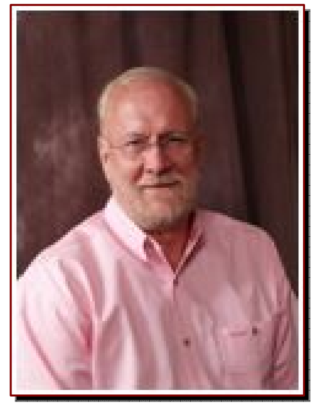
Whiteside & Associates

# TRANSPORTATION REPORT

To: **MONTANA WHEAT & BARLEY COMMITTEE**

From: Terry Whiteside

Date: July 28, 2009



## STB ISSUES A DECISION GRANTING $100 MILLION IN REPARATIONS AND RATE REDUCTIONS FOR EXCESSIVE UP RATES

The Surface Transportation Board issued a decision today granting an estimated $100 million in reparations and rate reductions over the next decade from the Union Pacific Railroad Company (UP) to Oklahoma Gas & Electric Company (OG&E). The utility serves more than 750,000 customers in Oklahoma and western Arkansas.

This is the second major decision by the STB in recent months (see February 18, 2009 Transportation Report) ordering roll backs to railroads excessively high freight rate charges. In February, 2009, the STB ordered BNSF to reduce rates in the largest single rate case in history by over $345 Million over the next ten years to the Laramie River Station of Basin Electric/Western Fuels because of excessively high freight rates.

UP has hauled roughly 6 million tons of coal per year from Wyoming's southern Powder River Basin to OG&E's Muskogee Station power plant in Fort Gibson, Okla. under contracts between the parties. But after the latest contract expired on Dec. 31, 2008, UP and OG&E could not agree on a new contractual rate. So OG&E asked UP for common carrier rates, which the utility began paying in January 2009. OG&E then challenged the new rates in a complaint to the Surface Transportation Board (STB).


Whiteside & Associates, 3203 Third Avenue North, Suite 301, Billings, MT 59101, Phone: 406-245-5132 email*:* *twhitesd@wtp.net*

Both OG&E and UP agreed that the Muskogee Station is captive to UP, meaning that there is no effective transportation alternative available to OG&E other than using UP. And both parties agreed that the January 2009 common carrier rates should not exceed 180 percent of the variable costs of providing that transportation. The central question put to the STB in this case centered on how to calculate the 180 percent revenue-to-variable cost ratio.

Once again the STB is relying on shipper and carrier agreement to establish the upper maximum rate levels at 180% for this unit train operation which is the jurisdictional threshold established in the law.

The STB found that the amount of relief owed to OG&E for the first two quarters of 2009 ranged from $1.66 to $1.91 per ton in shipper-supplied rail cars, depending on the particular mine origin. The decision also ordered UP to set common carrier rates for the next 10 years at the 180 percent of variable-costs levels. Assuming historical volumes of 6 million tons a year, the relief to OG&E will likely exceed $10 million a year for the next 10 years.

This was an important decision as the STB established the methodology for updating Uniform Rail Costing System (URCS) model costing by quarters. "Therefore, to determine the maximum lawful rates it may charge under this decision, UP must calculate variable costs in a given quarter by using the most recent URCS data indexed to that quarter by using the most recent AAR indices and PPI. UP should then combine those data with the actual operating characteristics to estimate a given movement's variable cost. This is the best estimate of variable cost that will be available at the beginning of a quarter. UP should then multiply the stipulated maximum lawful R/VC ratio by the variable costs to calculate the rate to be charged in that quarter. UP is directed to update the maximum lawful rate quarterly in order to reflect the most recent URCS data and indices. (For instance, when the Third Quarter PPI becomes available by November 1, 2009, UP will update the maximum lawful rate to reflect these data.) Thereafter, through the end of 2018, UP shall update the maximum lawful rate quarterly to reflect the most current URCS data and indices available.

The Board issued its decision on July 24, 2009, Oklahoma Gas & Electric Company v. Union Pacific Railroad, STB Docket No. 42111, http://www.stb.dot.gov/decisions/readingroom.nsf/WebDecisionID/39918?OpenDocument


Whiteside & Associates, 3203 Third Avenue North, Suite 301, Billings, MT 59101, Phone: 406-245-5132 email: *twhitesd@wtp.net*